United Nations A/CN.9/WG.V/WP.158

General Assembly

Distr.: Limited
26 February 2018

Original: English

United Nations Commission on International Trade Law
Working Group V (Insolvency Law)
Fifty-third session
New York, 7–11 May, 2018

Facilitating the cross-border insolvency of enterprise groups: draft legislative provisions

Note by the Secretariat

Contents

		Page
I.	Introduction	3
II.	Draft legislative provisions on facilitating the cross-border insolvency of enterprise groups	4
	Chapter 1. General provisions	4
	Preamble	4
	Article 1. Scope	4
	Article 2. Definitions	5
	Article 2 bis. Jurisdiction of the enacting State	6
	Article 2 ter. Public policy exception	6
	Article 2 quater. Competent court or authority	6
	Chapter 2. Cooperation and coordination	6
	Article 3. Cooperation and direct communication between a court of this State and foreign courts, foreign representatives and a group representative	6
	Article 4. Cooperation to the maximum extent possible under article 3	6
	Article 5. Limitation of the effect of communication under article 3	7
	Article 6. Coordination of hearings	7
	Article 7. Cooperation and direct communication between a group representative, foreign representatives and foreign courts	8

V.18-00979 (E)

Please recycle

Article 7 bis. Cooperation and direct communication between a [insert the title of a person or body administering a reorganization or liquidation with respect to an enterprise group member under the law of the enacting State], foreign courts, foreign representatives and a group representative 8

Article 8. Cooperation to the maximum extent possible under articles 7 and 7 bis 8

Article 9. Authority to enter into agreements concerning the coordination of proceedings 8

Article 10. Appointment of a single or the same insolvency representative 9

Article 11. Participation by enterprise group members in a proceeding under [*identify laws of the enacting State relating to insolvency*] 9

Chapter 3. Conduct of a planning proceeding in this State 10

Article 12. Appointment of a group representative 10

Article 13. Relief available to a planning proceeding 11

Chapter 4. Recognition of a foreign planning proceeding and relief 13

Article 14. Application for recognition of a foreign planning proceeding 13

Article 15. Provisional relief that may be granted upon application for recognition of a foreign planning proceeding 14

Article 16. Decision to recognize a foreign planning proceeding 15

Article 17. Relief that may be granted upon recognition of a foreign planning proceeding 16

Article 18. Participation of a group representative in a proceeding under [*identify laws of the enacting State relating to insolvency*] 17

Article 19. Protection of creditors and other interested persons 17

Article 20. Approval of local elements of a group insolvency solution 18

Chapter 5. Treatment of foreign claims 20

Article 21. Undertaking on the treatment of foreign claims: non-main proceedings 20

Article 21 bis. Powers of the court of this State with respect to an undertaking under article 21 20

Article 22. Undertaking on the treatment of foreign claims: main proceedings 21

Article 22 bis. Powers of a court of this State with respect to an undertaking under article 22 21

Article 23. Additional relief 22

I. Introduction

1. At its forty-fourth session in December 2013, following a three-day colloquium, the Working Group agreed to continue its work on the cross-border insolvency of enterprise groups[1] by developing provisions on a number of issues that would extend the existing articles of the UNCITRAL Model Law on Cross-Border Insolvency (MLCBI) and part three of the UNCITRAL Legislative Guide on Insolvency Law (the Legislative Guide), as well as involving reference to the UNCITRAL Practice Guide on Cross-Border Insolvency Cooperation. While the Working Group considered that those provisions might, for example, form a set of model provisions or a supplement to the existing MLCBI, it noted that the precise form they might take could be decided as the work progressed.

2. At its forty-fifth (April 2014), forty-sixth (December 2014) and forty-seventh (May 2015) sessions, the Working Group considered the goals of a text that might be developed to facilitate the cross-border insolvency of enterprise groups; the key elements of such a text, including those that might be based upon part three of the Legislative Guide and on MLCBI; and the form that the text might take, noting that some of the key elements lent themselves to being developed as a model law, while others were perhaps more in the nature of provisions that might be included in a legislative guide (A/CN.9/WG.V/WP.120, 124 and 128 respectively).

3. At its forty-eighth session (December 2015), the Working Group agreed a set of key principles for a regime to address cross-border insolvency in the context of enterprise groups (A/CN.9/WG.V/WP.133) and considered a number of draft provisions addressing three main areas (A/CN.9/WG.V/WP.134): (a) coordination and cooperation of insolvency proceedings relating to an enterprise group; (b) elements needed for the development and approval of a group insolvency solution involving multiple entities; and (c) the use of so-called "synthetic proceedings" in lieu of commencing non-main proceedings. Two additional supplemental areas were also considered. These might include (d) the use of so-called "synthetic proceedings" in lieu of commencing main proceedings, and (e) approval of a group insolvency solution on a more streamlined basis by reference to the adequate protection of the interests of creditors of affected group members.

4. At its forty-ninth session (May 2016), the Working Group considered a consolidated draft legislative text incorporating the agreed key principles and draft provisions addressing the five areas indicated in paragraph 3 (A/CN.9/WG.V/WP.137 and Add.1). That draft text was further considered at the fiftieth (December 2016), fifty-first (May 2017) and fifty-second (December 2017) sessions (A/CN.9/WG.V/WP.142 and Add.1; A/CN.9/WG.V/WP.146 and A/CN.9/WG.V/WP.152 respectively).

5. The draft text below reflects the discussion and decisions taken at the fifty-second session (A/CN.9/931) and revisions the Secretariat was requested to make, together with various suggestions and proposals arising from the Secretariat's work on the draft text.

General drafting issue

6. As a general drafting matter, the Working Group may wish to consider the form in which this draft text should be completed. If it is decided to retain the text as "Legislative Provisions", the references in some of the draft articles to "this Law" might need to be replaced (e.g., preamble and articles 1, 2 bis, 2 ter, 2 quater, 11 and 19). In addition, the relationship of this text to the UNCITRAL Model Law on Cross-Border Insolvency could be considered, particularly with respect to additional

[1] *Official Records of the General Assembly, Sixty-fifth Session, Supplement No. 17* (A/65/17), subpara. 259(a); A/CN.9/763, paras. 13–14; *Official Records of the General Assembly, Sixty-eighth Session, Supplement No. 17* (A/68/17), para. 326.

definitions that might be required if this draft text is to be a standalone text (see notes on article 2).

II. Draft legislative provisions on facilitating the cross-border insolvency of enterprise groups

[Part A]

Chapter 1. General Provisions

Preamble

The purpose of this Law is to provide effective mechanisms to address cases of cross-border insolvency affecting the members of an enterprise group, in order to promote the objectives of:

(a) Cooperation between courts and other competent authorities of this State and foreign States involved in cases of cross-border insolvency affecting members of an enterprise group;

(b) Cooperation between insolvency representatives appointed in this State and foreign States in cases of cross-border insolvency affecting members of an enterprise group;

(c) Development of a group insolvency solution for the whole or part of an enterprise group and cross-border recognition and implementation of that solution in multiple States;

(d) Fair and efficient administration of cross-border insolvencies concerning enterprise group members that protects the interests of all creditors and other interested persons, including the debtors;

(e) Protection and maximization of the overall combined value of the operations and assets of enterprise group members affected by insolvency and of the enterprise group as a whole;

(f) Facilitation of the rescue of financially troubled enterprise groups, thereby protecting investment and preserving employment; and

(g) Adequate protection of the interests of the creditors of each group member participating in a group insolvency solution.

Notes on the preamble

1. The substance of the preamble as drafted was approved at the fifty-second session (A/CN.9/931, para. 65). The Working Group may wish consider, to ensure consistent usage in the draft text, whether there is a need to reflect the two dimensions of subparagraph (e), that is the "overall combined value of the operations and assets of enterprise group members affected by insolvency ***and*** of the enterprise group as a whole" *[emphasis added]* in other articles which refer to the "overall combined value of the group members" but not to the group as a whole. These are article 2, subparagraph (f), the definition of "group insolvency solution" and article 14, subparagraph 3(c), which relates to the statement to accompany an application for recognition.

Article 1. Scope

This Law applies to enterprise groups, where insolvency proceedings have commenced for one or more of its members, [and addresses] [including] the conduct and administration of insolvency proceedings for those enterprise group members and cross-border cooperation between those proceedings.

Notes on article 1

2. Draft article 1 has been revised in accordance with the report of the fifty-second session (A/CN.9/931, para. 66), based upon what was previously variant 2 of article 1 in A/CN.9/WG.V/WP.152. The opening words have been revised and the words following "including" have been retained for further consideration. In view of the additional wording, the word "including" seems inapt and might be replaced by words such as "and addresses".

Article 2. Definitions

For the purposes of these provisions:

(a) "Enterprise" means any entity, regardless of its legal form, that is engaged in economic activities and may be governed by the insolvency law;

(b) "Enterprise group" means two or more enterprises that are interconnected by control or significant ownership;

(c) "Control" means the capacity to determine, directly or indirectly, the operating and financial policies of an enterprise;

(d) "Enterprise group member" means an enterprise that forms part of an enterprise group;

(e) "Group representative" means a person or body, including one appointed on an interim basis, authorized to act as a representative of a planning proceeding;

(f) "Group insolvency solution" means a set of proposals developed in a planning proceeding for the reorganization, sale, or liquidation of some or all of the operations or assets of one or more enterprise group members, with the goal of preserving or enhancing the overall combined value of the group members involved;

(g) "Planning proceeding" means an insolvency proceeding commenced in respect of an enterprise group member at its centre of main interests provided:

(i) One or more other enterprise group members are participating in that proceeding for the purpose of developing and implementing a group insolvency solution;

(ii) The enterprise group member subject to the proceeding is a necessary and integral part of that group insolvency solution; and

(iii) A group representative has been appointed.

Notes on article 2

3. Draft article 2 has been revised in accordance with the report of the fifty-second session (A/CN.9/931, paras. 67–75). Paragraphs (a), (b), (c) and (e) were approved as drafted; paragraph (d) has been shortened to remove unnecessary words; variant 2 of subparagraph (f) has been retained and subparagraph (g) has been redrafted in accordance with a proposal contained in paragraph 72 of A/CN.9/931.

4. The Working Group may wish to consider the drafting of subparagraph (f), in particular replacing the last phrase "the group members involved" with "those group members", which more clearly links that phrase with the preceding reference to "one or more enterprise group members" and removes the uncertainty created by the use of the word "involved". The Working Group may also wish to consider whether the phrase "and of the enterprise group as a whole", might, as raised in the notes on the preamble above, be added to subparagraph (f).

5. Additional definitions that might be added to the Legislative Provisions, depending on the final form of the text, might include: "court", "insolvency representative", "establishment", and "main" and "non-main" proceedings. These are terms used and defined in MLCBI and the Legislative Guide.

Article 2 bis. Jurisdiction of the enacting State

Where the centre of main interests of an enterprise group member is located in this State, nothing in this Law is intended to:

(a) Limit the jurisdiction of the courts of this State with respect to that enterprise group member;

(b) Limit any process or procedure (including any permission, consent or approval) required in this State in respect of that enterprise group member's participation in a group insolvency solution being developed in another State;

(c) Limit the commencement of insolvency proceedings in this State under [*identify laws of the enacting State relating to insolvency*], if required or requested to address the insolvency of that enterprise group member; or

(d) Create an obligation to commence insolvency proceedings [in respect of that enterprise group member] in this State when no such obligation exists.

Notes on article 2 bis

6. Article 2 bis has been revised in accordance with the report of the fifty-second session (A/CN.9/931, para. 76), in particular by revising subparagraph (d) to retain the last four words without square brackets.

7. The Working Group may wish to consider whether, to ensure consistent usage and drafting of the various subparagraphs, the words in square brackets in subparagraph (d) should be added; the other subparagraphs already refer to "that group member".

Article 2 ter. Public policy exception

Nothing in this Law prevents the court from refusing to take an action governed by this Law if the action would be manifestly contrary to the public policy of this State.

Article 2 quater. Competent court or authority

The functions referred to in this Law relating to the recognition of an insolvency proceeding or a planning proceeding and cooperation with foreign courts shall be performed by [*specify the court, courts, authority or authorities competent to perform those functions in the enacting State*].

Chapter 2. Cooperation and coordination

Article 3. Cooperation and direct communication between a court of this State and foreign courts, foreign representatives and a group representative

1. In the matters referred to in article 1, the court shall cooperate to the maximum extent possible with foreign courts, foreign representatives and a group representative, where appointed, either directly or through a [*insert the title of a person or body administering a reorganization or liquidation under the law of the enacting State*] or other person appointed to act at the direction of the court.

2. The court is entitled to communicate directly with, or to request information or assistance directly from, foreign courts, foreign representatives or a group representative, where appointed.

Article 4. Cooperation to the maximum extent possible under article 3

For the purposes of article 3, cooperation to the maximum extent possible may be implemented by any appropriate means, including:

(a) Communication of information by any means considered appropriate by the court;

(b) Participation in communication with a foreign court, a foreign representative or a group representative, where appointed;

(c) Coordination of the administration and supervision of the affairs of enterprise group members;

(d) Coordination of concurrent proceedings commenced with respect to enterprise group members;

(e) Appointment of a person or body to act at the direction of the court;

(f) Approval and implementation of agreements concerning the coordination of proceedings relating to two or more enterprise group members located in different States, including where a group insolvency solution is being developed;

(g) Cooperation among courts as to how to allocate and provide for the costs associated with cross-border cooperation and communication;

(h) Use of mediation or, with the consent of the parties, arbitration, to resolve disputes between enterprise group members concerning claims;

(i) Approval of the treatment of claims between enterprise group members;

(j) Recognition of the cross-filing of claims by or on behalf of enterprise group members and their creditors; and

(k) [*The enacting State may wish to list additional forms or examples of cooperation*].

Article 5. Limitation of the effect of communication under article 3

1. With respect to communication under article 3, the court is entitled at all times to exercise its independent jurisdiction and authority with respect to matters presented to it and the conduct of the parties appearing before it.

2. Participation by a court in communication pursuant to article 3, paragraph 2, does not imply:

(a) A waiver or compromise by the court of any powers, responsibilities or authority;

(b) A substantive determination of any matter before the court;

(c) A waiver by any of the parties of any of their substantive or procedural rights;

(d) A diminution of the effect of any of the orders made by the court;

(e) Submission to the jurisdiction of other courts participating in the communication; or

(f) Any limitation, extension or enlargement of the jurisdiction of the participating courts.

Article 6. Coordination of hearings

1. The court may conduct a hearing in coordination with a foreign court.

2. The substantive and procedural rights of the parties and the jurisdiction of the court may be safeguarded by the parties reaching agreement on the conditions to govern the coordinated hearing and the court approving that agreement.

3. Notwithstanding the coordination of the hearing, the court remains responsible for reaching its own decision on the matters before it.

Article 7. Cooperation and direct communication between a group representative, foreign representatives and foreign courts

1. A group representative appointed in this State shall, in the exercise of its functions and subject to the supervision of the court, cooperate to the maximum extent possible with foreign courts and foreign representatives of other enterprise group members to facilitate the development and implementation of a group insolvency solution.

2. A group representative is entitled, in the exercise of its functions and subject to the supervision of the court, to communicate directly with or to request information or assistance directly from foreign courts and foreign representatives of other enterprise group members.

Article 7 bis. Cooperation and direct communication between a [*insert the title of a person or body administering a reorganization or liquidation with respect to an enterprise group member under the law of the enacting State*], foreign courts, foreign representatives and a group representative

1. A [*insert the title of a person or body administering a reorganization or liquidation with respect to an enterprise group member under the law of the enacting State*] shall, in the exercise of its functions and subject to the supervision of the court, cooperate to the maximum extent possible with foreign courts, foreign representatives of other enterprise group members and a group representative, where appointed.

2. A [*insert the title of a person or body administering a reorganization or liquidation with respect to an enterprise group member under the law of the enacting State*] is entitled, in the exercise of its functions and subject to the supervision of the court, to communicate directly with or to request information or assistance directly from foreign courts, foreign representatives of other enterprise group members and a group representative, where appointed.

Article 8. Cooperation to the maximum extent possible under articles 7 and 7 bis

For the purposes of article 7 and article 7 bis, cooperation to the maximum extent possible may be implemented by any appropriate means, including:

(a) Sharing and disclosure of information concerning enterprise group members, provided appropriate arrangements are made to protect confidential information;

(b) Negotiation of agreements concerning the coordination of proceedings relating to two or more enterprise group members located in different States, including where a group insolvency solution is being developed;

(c) Allocation of responsibilities between a [*insert the title of a person or body administering a reorganization or liquidation with respect to an enterprise group member under the law of the enacting State*], a foreign representative and a group representative, where appointed;

(d) Coordination of the administration and supervision of the affairs of the enterprise group members; and

(e) Coordination with respect to the development and implementation of a group insolvency solution, where applicable.

Article 9. Authority to enter into agreements concerning the coordination of proceedings

A [*insert the title of a person or body administering a reorganization or liquidation with respect to an enterprise group member under the law of the enacting State*] may enter into an agreement concerning the coordination of proceedings involving two or more enterprise group members located in different States, including where a group insolvency solution is being developed.

Article 10. Appointment of a single or the same insolvency representative

1. The court may coordinate with foreign courts with respect to the appointment and recognition of a single or the same insolvency representative to administer and coordinate insolvency proceedings concerning members of the same enterprise group in different States.

2. The appointment of an insolvency representative in this State and in another State under paragraph 1 does not diminish the obligations of the insolvency representative under the law of this State.

Notes on articles 2ter to 10

8. The substance of those articles as drafted was approved at the fifty-second session (A/CN.9/931, paras. 77–87). Sharing of information and protection of confidentiality under article 8 and potential conflicts of interest under article 10 will be addressed in the draft guide to enactment of those articles.

9. The Working Group may wish to consider several issues:

(a) Whether there is a need in articles 7 and 7bis to include the possibility that cooperation and direct communication might also concern (i) in article 7, an insolvency representative appointed for a group member in the same State as the group representative, and (ii) in article 7 bis, several insolvency representatives appointed for a group members in the enacting State; and

(b) Whether, under article 9, a group representative might also enter into an agreement of the type mentioned; article 8 would seem to suggest that possibility is contemplated.

Article 11. Participation by enterprise group members in a proceeding under [*identify laws of the enacting State relating to insolvency*]

1. Subject to paragraph 2, if a proceeding under [*identify laws of the enacting State relating to insolvency*] has commenced with respect to an enterprise group member whose centre of main interests is located in this State, any other enterprise group member may participate in that proceeding for the purpose of facilitating cooperation and coordination under chapter 2 of this Law, including developing and implementing a group insolvency solution.

2. An enterprise group member whose centre of main interests is located in another State may participate in a proceeding referred to in paragraph 1 unless a court in that other State prohibits it from so doing.

3. The sole fact that an enterprise group member is participating in a proceeding referred to in paragraph 1 does not subject the enterprise group member to the jurisdiction of the courts of this State for any purpose unrelated to that participation.

3 bis. Participation means that the enterprise group member has the right to appear, make written submissions and be heard in that proceeding on matters affecting that enterprise group member's interests and to take part in the development and implementation of a group insolvency solution.

4. Participation by any other enterprise group member in a proceeding referred to in paragraph 1 is voluntary. An enterprise group member may commence its participation or opt out of participation at any stage of such a proceeding.

5. A participating enterprise group member shall be notified of actions taken with respect to the development of a group insolvency solution.

Notes on article 11

10. Article 11 has been revised in accordance with the report of the fifty-second session (A/CN.9/931, paras. 88–90): the words "for the purpose of facilitating cooperation and coordination under chapter 2" have been added to paragraph 1,

together with the words "of this Law" to clarify the reference (see the note in para. 6 of the Introduction to this paper) and the words "for the purpose of" that followed the word "including" have been deleted. Paragraph 3 has been revised, taking into account article 10 of MLCBI, to provide greater certainty and clarity with respect to the limited jurisdiction intended by the provision. The description of what constitutes participation has been separated from paragraph 3 and placed in new paragraph 3bis. Limits that might be applicable under domestic law to a group member's ability to opt in or out of participation in a planning proceeding under paragraph 4 will be addressed in the draft guide to enactment of this article.

Chapter 3. Conduct of a planning proceeding in this State

Article 12. Appointment of a group representative

1. When one or more enterprise group members participate in a proceeding referred to in article 11, and the requirements of article 2, subparagraphs (g)(i) and (ii) are [otherwise] met, the court may appoint a group representative, by which the proceeding becomes a planning proceeding.

2 [3].A group representative is authorized to seek relief in this State to support the development and implementation of a group insolvency solution.

3 [4].A group representative is authorized to act in a foreign State on behalf of a planning proceeding and, in particular, to:

(a) Seek recognition of the planning proceeding and relief to support the development and implementation of the group insolvency solution;

(b) Seek to participate in a foreign proceeding relating to an enterprise group member participating in the planning proceeding; and

(c) Seek to participate in a foreign proceeding relating to an enterprise group member not participating in the planning proceeding.

Notes on article 12

11. Article 12 has been revised in accordance with the report of the fifty-second session (A/CN.9/931, para. 91), adding the references in the chapeau to subparagraphs (g)(i) and (g)(ii); deleting subparagraph 2; removing the square brackets from around paragraph 3 (now para. 2) and deleting the text "as permitted by the applicable foreign law" previously in square brackets in paragraph 4 (now para. 3).

12. The Working Group may wish to consider the following drafting changes:

(a) The word "otherwise" in paragraph 1 might be deleted as it creates some uncertainty as to what is intended; and

(b) The references in subparagraphs (b) and (c) to a "foreign proceeding" (which is not currently a defined term) might need to be expanded to make it clear whether they are intended to refer to proceedings commenced under the laws of the foreign State relating to insolvency or more generally to any proceeding relating to an enterprise group member. The substance of article 18, which is the inbound provision complementary to subparagraph 3(b) which authorizes that participation in the foreign State, would suggest that the same drafting should be used in article 12, subparagraphs 3(b) and possibly 3(c) (although noting that there is no inbound authorization in article 18 equivalent to article 12, subparagraph 3(c), as it was previously deleted (see A/CN.9/903, para. 125 and A/CN.9/931, para. 92)).

Article 13. Relief available to a planning proceeding

1. To the extent needed to preserve the possibility of developing or implementing a group insolvency solution or to protect the assets of an enterprise group member subject to or participating in a planning proceeding or the interests of the creditors of such an enterprise group member, the court, at the request of the group representative, may grant any of the following relief:

(a) Staying execution against the assets of the enterprise group member;

(b) Suspending the right to transfer, encumber, or otherwise dispose of any assets of the enterprise group member;

(c) Staying any insolvency proceedings concerning a participating enterprise group member;

(d) Staying the commencement or continuation of individual actions or individual proceedings concerning the assets, rights, obligations, or liabilities of the enterprise group member;

(e) Entrusting the administration or realization of all or part of the assets of the enterprise group member located in this State to the group representative or another person designated by the court, in order to protect and preserve the value of assets that, by their nature or because of other circumstances, are perishable, susceptible to devaluation, or otherwise in jeopardy;

(f) Providing for the examination of witnesses, the taking of evidence, or the delivery of information concerning the assets, affairs, rights, obligations, or liabilities of the enterprise group member;

(g) Recognizing arrangements concerning the funding of enterprise group members participating in the planning proceeding where the funding entity is located in this State and authorizing the provision of finance under those funding arrangements, subject to any appropriate safeguards the court may apply; and

(h) Granting any additional relief that may be available to [*insert the title of a person or body administering a reorganization or liquidation under the law of the enacting State*] under the laws of this State.

2. Relief under this article may not be granted with respect to the assets and operations located in this State of any enterprise group member participating in a planning proceeding if that enterprise group member is not subject to insolvency proceedings [unless not commencing an insolvency proceeding is a consequence of an undertaking given under articles 21 or 22].

3. With respect to the assets or operations located in this State of an enterprise group member that has its centre of main interests in another State, relief under this article may only be granted if that relief does not interfere with the [conduct and] administration of insolvency proceedings taking place in that State.

Notes on article 13

13. Article 13 has been revised in accordance with the report of the fifty-second session (A/CN.9/931, paras. 56 and 93); aligning paragraph 2 with the equivalent paragraphs of articles 15 and 17 and deleting the square brackets around "or implementing" in paragraph 1.

Subparagraph (c)

14. Subparagraphs (c) and (g), unlike the other subparagraphs of the draft article, concern only those group members participating in a planning proceeding. For that reason, it may improve the drafting if subparagraph (c) was to be placed at the end of paragraph 1. That might avoid any confusion in the subparagraphs that follow subparagraph (c) and refer to "the group member", meaning the group member as

referred to in the chapeau of paragraph (both "subject to" and "participating in" the planning proceeding) rather than the group member referred to in subparagraph (c).

Subparagraph 1(g)

15. The drafting of subparagraph (g) could be aligned with the drafting used in subparagraph (c) which refers, in the singular, to "a participating group member". In that case, the drafting of subparagraph (g) could be "Recognizing arrangements concerning the funding of a participating enterprise group member where the funding entity is located in this State and authorizing the provision of finance under those funding arrangements, subject to any appropriate safeguards the court may apply" (see also article 15, subparagraph 1(g) and article 17, subparagraph(h)).

16. The proviso in article 13, subparagraph (g), "subject to any appropriate safeguards the court may apply" is already contained in article 19, paragraph 2, and thus may not be required in article 13. The guide to enactment of article 13 could draw attention to the relevance of article 19, paragraph 2. This observation applies to the same drafting in articles 15, subparagraph 1(g) and 17, subparagraph 1(h).

Paragraph 3

17. The Working Group may wish to consider whether the words in square brackets "[conduct and]" in article 13, paragraph 3, should be deleted to align the drafting with article 15, paragraph 5 and article 17, paragraph 4.

Issue for consideration with respect to the relief provisions — articles 13, 15 and 17

18. The Working Group may wish to consider the following scenario in terms of the application of the relief articles — article 13, paragraph 2, article 15, paragraph 4, article 17, paragraph 3, and article 23, paragraph 1.

> Four members of an enterprise group have their respective COMIs in States A, B, C, and D. All four group members are insolvent. All four States have enacted articles 1–21 of the Legislative Provisions, but only C and D have enacted articles 22 and 23.
>
> A proceeding in State A becomes a planning proceeding, and the other three group members all choose to participate. The group representative seeks, and is granted, recognition of the A planning proceeding in B, C, and D. In C, the court uses article 23, paragraph 1 to decline to open a main proceeding for the insolvent group member with its COMI in C, on the basis that the A planning proceeding will adequately protect the interests of creditors. The court sees no need to commence a proceeding in C at this stage, given that the development of a group solution seems likely. Articles 21 and 22 have not been used in any of the States.
>
> In that situation, none of the remaining States A, B or D — regardless of whether they are the location of the planning proceeding (A) or have enacted the supplemental provisions (D) — would be able to grant any relief (whether interim or otherwise) with respect to establishments or assets of the C entity in their territories. The court in A would be precluded from ordering such relief under article 13, paragraph 2 because no insolvency proceeding has been commenced for the C entity and no undertaking has been given under article 21 or 22. For similar reasons, the courts in B and D could not use article 15, paragraph 4 to provide interim relief or article 17, paragraph 3 to provide relief following recognition of the planning proceeding.

19. If the entity in C is important for the group solution to work, States A and B in the hypothetical may wish to be able to grant relief if needed; it might be asserted that C's choice to enact and use article 23, paragraph 1 shouldn't effectively preclude other States from using articles 13, 15 and 17 as needed within their own territories.

20. Various solutions might be considered. The first could be to address that issue through the drafting used in article 13, paragraph 2 (and arts. 15, para. 4 and 17, para. 3) to address the prohibition on ordering relief with respect to the assets of what are, essentially, "solvent" entities. The more neutral drafting of "not subject to insolvency proceedings" was used to avoid use of the word "solvent" (given the difficulty of reaching an agreed definition) and the need for the court to resolve the question of whether a particular entity was solvent. It does not, however, sufficiently describe an exception that is intended to reflect the financial status of the group member and the fact that it is not subject to the insolvency law on the basis of that status.

21. Another solution might be to describe the entity as "solvent" (with the guide to enactment explaining what the use of that word is intended to convey), in which case the proviso ("unless not commencing ...") may not be required. The problem posed in the hypothetical above would not arise.

22. A further solution might be to add a reference to article 23 in the proviso. In that case, it might be helpful to refer to articles 21bis, 22bis and 23 (rather than articles 21, 22 and 23) on the basis that it is those articles that directly address the power of the court to decline to commence a proceeding. The proviso might thus be revised along the lines of "unless a [competent] court has declined to commence an insolvency proceeding with respect to that group member under article 21bis, 22bis or 23." That drafting would address the problem posed by the hypothetical, albeit from a different angle unrelated to the financial status of the "solvent" group member.

Chapter 4. Recognition of a foreign planning proceeding and relief

Article 14. Application for recognition of a foreign planning proceeding

1. A group representative may apply in this State for recognition of the planning proceeding to which the group representative was appointed.

2. An application for recognition shall be accompanied by:

(a) A certified copy of the decision appointing the group representative; or

(b) A certificate from the foreign court affirming the appointment of the group representative; or

(c) In the absence of evidence referred to in subparagraphs (a) and (b), any other evidence acceptable to the court of the appointment of the group representative.

3. An application for recognition shall also be accompanied by:

(a) A statement identifying each enterprise group member participating in the planning proceeding;

(b) A statement identifying all members of the enterprise group and all proceedings commenced in respect of enterprise group members participating in the planning proceeding that are known to the group representative; and

(c) A statement to the effect that the enterprise group member subject to the planning proceeding has its centre of main interests in the State where the planning proceeding is taking place and that that proceeding is likely to result in added overall combined value for the enterprise group members subject to or participating in that proceeding.

4. The court may require a translation of documents supplied in support of the application for recognition into an official language of this State.

Notes on article 14

23. Article 14 has been revised in accordance with the report of the fifty-second session (A/CN.9/931, paras. 53–55). The drafting clarifies that the subparagraphs in paragraph 2 are alternatives; the previous requirement for "evidence" in subparagraph 3(a) has been replaced with a requirement for "a statement"; and the word "involved"

at the end of subparagraph 3(c) has been replaced by a reference to those group members subject to or participating in the planning proceeding. The draft guide to enactment will explain the difference between those two categories of group members.

Subparagraph (b)

24. For greater clarity, it may be helpful to add the word "insolvency" before the first reference to "proceedings" in subparagraph (b), if the subparagraph is intended to be limited in that manner. It may also be helpful to clarify whether the words "are known to the group representative" refer to the enterprise group members known to the group representative or to the proceedings known to the group representative, or both.

Subparagraph (c)

25. With respect to the statement on overall value in subparagraph (c), see the note above with respect to the preamble.

Article 15. Provisional relief that may be granted upon application for recognition of a foreign planning proceeding

1. From the time of filing an application for recognition [of a planning proceeding] until the application is decided upon, where relief is urgently needed to preserve the possibility of developing or implementing a group insolvency solution or to protect the assets of an enterprise group member subject to or participating in a planning proceeding or the interests of the creditors of such an enterprise group member, the court may, at the request of the group representative, grant relief of a provisional nature, including:

(a) Staying execution against the assets of the enterprise group member;

(b) Suspending the right to transfer, encumber, or otherwise dispose of any assets of the enterprise group member;

(c) Staying any insolvency proceedings concerning the enterprise group member;

(d) Staying the commencement or continuation of individual actions or individual proceedings concerning the assets, rights, obligations, or liabilities of the enterprise group member;

(e) In order to protect and preserve the value of assets that, by their nature or because of other circumstances, are perishable, susceptible to devaluation, or otherwise in jeopardy, entrusting the administration or realization of all or part of the assets of the enterprise group member located in this State to an insolvency representative appointed in this State. Where that insolvency representative is not able to administer or realize all or part of the assets of the enterprise group member located in this State, the group representative or another person designated by the court may be entrusted with that task;

(f) Providing for the examination of witnesses, the taking of evidence, or the delivery of information concerning the assets, affairs, rights, obligations, or liabilities of the enterprise group member;

(g) Recognizing arrangements concerning the funding of enterprise group members participating in the planning proceeding where the funding entity is located in this State and authorizing the provision of finance under those funding arrangements, subject to any appropriate safeguards the court may apply; and

(h) Granting any additional relief that may be available to [*insert the title of a person or body administering a reorganization or liquidation under the law of the enacting State*] under the laws of this State.

2. [*Insert provisions of the enacting State relating to notice.*]

3. Unless extended under article 17, subparagraph 1(a), the relief granted under this article terminates when the application for recognition is decided upon.

4. Relief under this article may not be granted with respect to the assets and operations located in this State of any enterprise group member participating in a planning proceeding if that group member is not subject to insolvency proceedings [unless not commencing an insolvency proceeding is a consequence of an undertaking given under articles 21 or 22].

5. The court may refuse to grant relief under this article if such relief would interfere with the administration of an insolvency proceeding taking place in the centre of main interests of an enterprise group member participating in the planning proceeding.

Notes on article 15

26. Article 15 has been revised in accordance with the report of the fifty-second session (A/CN.9/931, paras. 56–57). The title has been revised to refer to "Provisional" relief; the word "appropriate" has been deleted from the chapeau; the words "in any jurisdiction" have been deleted at the end of paragraph 4 and the words in square brackets have been added at the end of paragraph 4, in response to the issue raised in document A/CN.9/WG.V/WP.152, para. 21, for further consideration (see also the note under article 13 relating to the relief provisions and the drafting of the proviso in para. 4).

27. The Working Group may wish to note it was agreed at its fifty-second session (A/CN.9/931, para. 57), that additional analysis was required to ensure that that draft text would address situations arising in connection with paragraph 4 in which articles 21 and 22 did not apply.

Paragraph 1

28. The words "of a planning proceeding" might be added to paragraph 1 as indicated.

Subparagraph 1(e)

29. An issue to be considered with respect to subparagraph 1(e) is whether the existing language ("Where an insolvency representative is not able to administer or realize ...") would be sufficient to address the situation where no insolvency representative was appointed in the enacting State (e.g., because article 21 bis or 22 bis is applicable) and whether further language along the lines of "or no insolvency representative has been appointed" might be required, for example, in the second sentence.

Subparagraph 1(g)

30. With respect to the drafting of subparagraph 1(g), see the note above concerning the drafting of article 13, subparagraph 1(g).

31. The proviso in article 15, subparagraph 1(g) "subject to any appropriate safeguards the court may apply" is already covered by article 19, paragraph 2 and thus may not need to be repeated in article 15. The guide to enactment of article 15 could ensure the relevance of article 19 is highlighted. As noted above with respect to article 13, this observation applies also to articles 13 and 17.

Article 16. Decision to recognize a foreign planning proceeding

1. Subject to article 2 ter, a planning proceeding shall be recognized if:

(a) The application meets the requirements of article 14, paragraphs 2 and 3;

(b) The proceeding is a planning proceeding within the meaning of article 2, subparagraph (g); and

(c) The application has been submitted to the court referred to in article 2 quater.

2. An application for recognition of a planning proceeding shall be decided upon at the earliest possible time.

3. Recognition may be modified or terminated if it is shown that the grounds for granting it were fully or partially lacking or have ceased to exist.

4. For the purposes of paragraph 3, the group representative shall inform the court of material changes in the status of the planning proceeding or in the status of its own appointment occurring after the application for recognition is made, as well as changes that might bear upon the relief granted on the basis of recognition.

Notes on article 16

32. On the basis that paragraph 1 lists the elements to be satisfied to grant recognition, the Working Group may wish to consider whether a further requirement might be added to paragraph 1 to reflect the approach taken by the drafting of article 17, subparagraph 1(b) of MLCBI, that is, that the group representative applying for recognition should be a group representative within the meaning of article 2, subparagraph (e) or whether article 14 is sufficient addresses that issue in the context of an application for recognition.

33. Article 16, paragraph 4 has been revised in accordance with the report of the fifty-second session (A/CN.9/931, para. 58): the word "material" has been retained in paragraph 4 and the words "as well as" have been added before the word "changes" in the final phrase of that paragraph.

Article 17. Relief that may be granted upon recognition of a foreign planning proceeding

1. Upon recognition of a planning proceeding, where necessary to preserve the possibility of developing or implementing a group insolvency solution or to protect the assets of an enterprise group member subject to or participating in the planning proceeding or the interests of the creditors of such an enterprise group member the court, at the request of the group representative, may grant any of the following relief:

(a) Extending any relief granted under article 15, paragraph 1;

(b) Staying execution against the assets of the enterprise group member;

(c) Suspending the right to transfer, encumber, or otherwise dispose of any assets of the enterprise group member;

(d) Staying any insolvency proceedings concerning the enterprise group member;

(e) Staying the commencement or continuation of individual actions or individual proceedings concerning the assets, rights, obligations, or liabilities of the enterprise group member;

(f) In order to protect and preserve the value of assets that, by their nature or because of other circumstances, are perishable, susceptible to devaluation, or otherwise in jeopardy, entrusting the administration or realization of all or part of the assets of the enterprise group member located in this State to an insolvency representative appointed in this State. Where that insolvency representative is not able to administer or realize all or part of the assets of the enterprise group member located in this State, the group representative or another person designated by the court may be entrusted with that task;

(g) Providing for the examination of witnesses, the taking of evidence, or the delivery of information concerning the assets, affairs, rights, obligations, or liabilities of the enterprise group member;

(h) Recognizing arrangements concerning the funding of enterprise group members participating in the planning proceeding where the funding entity is located in this State and authorizing the provision of finance under those funding arrangements, subject to any appropriate safeguards the court may apply; and

(i) Granting any additional relief that may be available to [*insert the title of a person or body administering a reorganization or liquidation under the law of the enacting State*] under the laws of this State.

2. In order to protect and preserve the value of assets that, by their nature or because of other circumstances, are perishable, susceptible to devaluation, or otherwise in jeopardy, entrusting the distribution of all or part of the enterprise group member's assets located in this State to an insolvency representative appointed in this State. Where that insolvency representative is not able to administer or realize all or part of the assets of the enterprise group member located in this State, the group representative or another person designated by the court may be entrusted with that task.

3. Relief under this article may not be granted with respect to the assets and operations located in this State of any enterprise group member participating in a planning proceeding if that enterprise group member is not subject to insolvency proceedings [unless not commencing an insolvency proceeding is a consequence of an undertaking given under articles 21 or 22].

4. The court may refuse to grant relief under this article if such relief would interfere with the administration of an insolvency proceeding taking place in the centre of main interests of an enterprise group member participating in the planning proceeding.

Notes on article 17

34. Article 17 has been revised in accordance with the report of the fifty-second session (A/CN.9/931, paras. 56, 60 and 93), deleting the words "in any jurisdiction" and adding the words in square brackets at the end of paragraph 3 in order to conform article 17 with articles 13 and 15.

Subparagraph 1(h)

35. See the note with respect to the drafting of the equivalent subparagraph in article 13 (subparagraph 1(g)) and 15 (subparagraph 1(e)) above.

Article 18. Participation of a group representative in a proceeding under [*identify laws of the enacting State relating to insolvency*]

Upon recognition of a planning proceeding, the group representative may participate in any proceeding under [*identify laws of the enacting State relating to insolvency*] concerning enterprise group members that are participating in the planning proceeding.

Notes on article 18

36. The substance of article 18 as drafted was approved at the fifty-second session (A/CN.9/931, para. 61).

Article 19. Protection of creditors and other interested persons

1. In granting, denying, modifying or terminating relief under this Law, the court must be satisfied that the interests of the creditors and other interested persons, including the enterprise group member subject to the relief to be granted, are adequately protected.

2. The court may subject relief granted under this Law to conditions it considers appropriate, including the provision of security.

3. The court may, at the request of the group representative or a person affected by relief granted under this Law, or at its own motion, modify or terminate such relief.

Notes on article 19

37. The substance of article 19 as drafted was approved at the fifty-second session (A/CN.9/931, para. 62).

38. Article 19 raises issues that are also addressed in the Preamble, subparagraph (g) and article 23, concerning the identity of creditors whose interests are to be protected. The Preamble, subparagraph (g), refers to adequate protection of the interests of the "creditors of each group member" participating in the group solution, thereby recognising the integrity of the individual group member and the fundamental importance of protecting its particular creditors within the enterprise group and the group insolvency solution. Article 19, paragraph 1, does not seem to draw this distinction, referring generally to "the creditors". In addition to the lack of certainty arising from that drafting, it may create a possibility that the interests of one group member's creditors could be traded off against the aggregated interests of the creditors of all participating members. This would appear to interfere with the separate legal identity of group members, and might tend to discourage participation in group solutions.

39. Additionally, article 19, paragraph 1, seeks to protect the interests of the group member itself (not just its creditors and others interested in it) as a separate criterion to be satisfied. This is not reflected in subparagraph (g) of the Preamble (although it may be reflected in part in subparagraph (d) of the Preamble by the reference to protection of the interests of debtors). The Working Group may wish to consider (a) whether the requirement to protect the interests of the group member itself is unnecessary and poses an additional hurdle to be overcome in order for the court to grant relief; and (b) what interests a group member would have that are distinctly different from the interests of its creditors and warrant be separate protection.

40. Any revision of article 19 might take into account article 23, which refers to protecting the interests of creditors of affected group members participating in a planning proceeding.

Article 20. Approval of [local elements of] a group insolvency solution

Variant 1 of paragraph 1

1. Where a group insolvency solution affects an enterprise group member participating in a planning proceeding that has its centre of main interests or establishment in this State and a proceeding under [*identify the laws of the enacting State relating to insolvency*] has commenced in this State, the group insolvency solution shall be submitted to the court in this State for approval.

Variant 2 of paragraph 1

1. When a proceeding under [*identify the laws of the enacting State relating to insolvency*] has commenced in this State with respect to an enterprise group member that (a) has it centre of main interests or establishment in this State, (b) is participating in a planning proceeding, and (c) is affected by a group insolvency solution, the group insolvency solution shall be submitted to the court in this State for approval.

2. The court shall refer the portion of the group solution affecting the enterprise group member referred to in paragraph 1 for approval in accordance with [*identify the laws of the enacting State relating to insolvency*].

3. If the approval process referred to in paragraph 2 results in approval of the relevant portion of the group insolvency solution, the court shall [confirm that portion relating to assets or operations in this State] [*specify the role to be played by the court in accordance with the law of the enacting State with respect to approval of a reorganization plan*].

Variant 1 of paragraph 4

4. Where a group solution affects an enterprise group member participating in the planning proceeding that has its centre of main interests or establishment in this State and no proceeding under [*identify the laws of the enacting State relating to insolvency*] has commenced in this State or article 21 applies, no such proceeding needs to be commenced if unnecessary to confirm the portion of the group insolvency solution affecting the enterprise group member.

Variant 2 of paragraph 4

4. When no proceeding under [*identify the laws of the enacting State relating to insolvency*] has commenced in this State with respect to an enterprise group member that (a) has it centre of main interests or establishment in this State, (b) is participating in a planning proceeding, and (c) is affected by a group insolvency solution, or article 21 applies, no such proceeding needs to be commenced if unnecessary to confirm the portion of the group insolvency solution affecting the enterprise group member.

4 bis. A group insolvency solution shall have effect in this State if it has received all approvals required in accordance with the laws of this State.

4 ter. A group representative may request additional assistance under other laws of this State to confirm the portion of the group insolvency solution affecting the enterprise group member.

5. A group representative is entitled to apply directly to a court in this State to be heard on issues related to approval and implementation of a group insolvency solution.

Notes on article 20

41. Article 20 has been revised in accordance with the report of the fifty-second session (A/CN.9/931, paras. 63–64).

Title

42. The Working Group may wish to consider whether the title of the article might be simplified to "Approval of a group insolvency solution".

Relevance of recognition to article 20

43. It might be noted that while article 20 appears in chapter 4 dealing with recognition of a planning proceeding, article 20 itself makes no reference to recognition of a planning proceeding as a pre-condition for either seeking approval of a group insolvency solution or for the group representative to apply directly to the court to be heard on issues relating to approval and implementation of the solution under article 20, paragraph 5. The Working Group may wish to consider whether recognition is required in order to seek approval of a group insolvency solution; if not, that issue might be addressed in the guide to enactment.

Paragraph 1

44. Variant 2 of paragraph 1 attempts to give greater clarity to the three conditions concerning the group member that will lead to submission of the group insolvency solution for approval in the enacting State. It applies to the situation where an insolvency proceeding concerning the affected group member has commenced in the enacting State.

Paragraph 3

45. Paragraph 3 retains two alternative approaches to approval of a group insolvency solution — the first requires confirmation by the court, the second leaves it up to the law of the enacting State to specify the role to be played by the court. Not all States require court confirmation of a reorganization plan approved in accordance with domestic law (e.g. by creditors), as recognized by the Legislative Guide on

Insolvency Law (part two, chapter IV, paras. 56–65). If the two alternatives are retained, the use of the word "confirm" in paragraph 4ter may need to be reconsidered. Moreover, for jurisdictions that do not require "confirmation" in a domestic setting, it may not be clear what is required in the Legislative Provisions by way of "confirmation"; this could be explained in the guide to enactment along the lines of, or by reference to, the material in the Legislative Guide.

Paragraph 4

46. Variant 2 of paragraph 4 uses the same approach to drafting as Variant 2 of paragraph 1 in the situation in which no proceeding has commenced in the enacting State. Paragraph 4bis reflects additional text approved by the Working Group at its fifty-second session (A/CN.9/931, para. 64). Paragraph 4ter, previously 4bis, has been slightly revised to refer to confirmation rather than implementation of a group insolvency solution (A/CN.9/931, para. 64).

Paragraph 5

47. Consideration might be given to whether article 20, paragraph 5 might be moved to article 12, paragraph 4, which identifies the activities the group representative is authorized to conduct. This would have the advantage of placing related provisions on the powers of the group representative together in the same article. The guide to enactment could provide relevant explanation.

Chapter 5. Treatment of foreign claims

Article 21. Undertaking on the treatment of foreign claims: non-main proceedings

1. To minimize the commencement of non-main proceedings and facilitate the treatment of claims in an enterprise group insolvency, a claim that could be brought by a creditor of an enterprise group member in a non-main proceeding in another State may be treated in a main proceeding commenced in this State in accordance with the treatment it would be accorded in the non-main proceeding, provided:

(a) An undertaking to accord such treatment is given by the insolvency representative appointed in the main proceeding in this State. Where a group representative is appointed, the undertaking should be given jointly by the insolvency representative and the group representative;

(b) The undertaking meets the formal requirements, if any, of this State; and

(c) The court approves the treatment to be accorded in the main proceeding.

2. An undertaking given under paragraph 1 shall be enforceable and binding on the insolvency estate.

Notes on article 21

48. Article 21 has been revised in accordance with the report of the fifty-second session (A/CN.9/931, paras. 45–47), based upon variant 2 of the text contained in document A/CN.9/WG.V/WP.152 and a proposal for redrafting the article as set forth in document A/CN.9/931, para. 46. The heading has been aligned with the revised article. It may be helpful to add the words "of the enterprise group member" at the end of paragraph 2 for greater clarity.

Article 21 bis. Powers of the court of this State with respect to an undertaking under article 21

If a foreign representative of an enterprise group member or a group representative from another State in which a main proceeding is pending has given an undertaking in accordance with article 21, a court in this State, may:

(a) Approve the treatment to be provided in the foreign main proceeding to the claims of creditors located in this State; and

(b) Stay or decline to commence a non-main proceeding.

Notes on article 21 bis

49. Article 21 bis has been revised in accordance with the report of the fifty-second session (A/CN.9/931, para. 48), based upon variant 2 of the text contained in document A/CN.9/WG.V/WP.152. The word "commitment" has been replaced with the word "undertaking" and the cross-reference to article 19 deleted (the relevance of article 19 will be addressed in the guide to enactment).

[Part B]

Supplemental provisions

Article 22. Undertaking on the treatment of foreign claims: main proceedings

To facilitate the treatment of claims that could otherwise be brought by a creditor in a[n insolvency] proceeding in another State, an insolvency representative of an enterprise group member or a group representative appointed in this State may undertake, and the court in this State may approve, to accord that claim the treatment in this State that it would have received in a[n insolvency] proceeding in that other State. Such undertaking shall be subject to the formal requirements, if any, of this State and shall be enforceable and binding on the insolvency estate.

Notes on article 22

50. Article 22 has been revised in accordance with the report of the fifty-second session (A/CN.9/931, para. 50). The word "would" in the first line has been replaced with the word "could", the word "commitment" has been replaced with the word "undertaking", the reference to the treatment of creditors has been replaced with a reference to the treatment of claims. The heading has been aligned with the revised article.

51. Replacing the word "commitment" with the word "undertaking" makes the drafting of the phrase "may undertake, and the court in this State may approve, to accord" somewhat awkward in English. A solution may be to place the reference to approval by the court in a separate sentence along the lines of "The court may approve the treatment to be accorded by the undertaking." An alternative approach would be delete any reference to approval by the court from article 22 on the basis that it is already covered by article 22bis.

52. Articles 21 and 21bis have been revised to make it clear that they refer to an undertaking given to avoid or minimize the commencement of non-main proceedings. While article 22 is intended to refer to avoiding the commencement of main proceedings, there is nothing in the drafting that specifically indicates that intent and it is unclear how it differs from article 21. As currently drafted, the reference to the "proceeding in another State" could be either a non-main proceeding, in which case the article repeats the content of article 21, or it could be a main proceeding, in which case it is different. The Working Group may wish to consider whether any further clarification is required, including adding "insolvency" before the word "proceeding" as indicated.

Article 22 bis. Powers of a court of this State with respect to an undertaking under article 22

If a foreign representative of an enterprise group member or a group representative from another State in which a[n insolvency] proceeding is pending has given an undertaking under article 22, a court in this State may:

(a) Approve the treatment in the foreign proceeding of the claims of creditors located in this State; and

(b) Stay or decline to commence a main proceeding.

Notes on article 22 bis

53. Article 22 bis has been revised in accordance with the report of the fifty-second session (A/CN.9/931, para. 51), based upon variant 2 of the text contained in document A/CN.9/WG.V/WP.152. The word "commitment" has been replaced with the word "undertaking" and the cross-reference to article 19 deleted. The Working Group may wish to consider whether "insolvency" should be added before the word "proceeding" as indicated.

Article 23. Additional relief

1. If, upon recognition of a planning proceeding, the court is satisfied that the interests of the creditors of affected enterprise group members would be adequately protected in [the planning] [that] proceeding, particularly where an undertaking under article 21 or 22 has been given, the court, in addition to granting any relief described in article 17, may stay or decline to commence insolvency proceedings in this State relating to any enterprise group member participating in the planning proceeding.

2. Notwithstanding article 20, if, upon submission of a proposed group insolvency solution by the group representative, the court is satisfied that the interests of the creditors of the affected enterprise group member [are] [or will be] adequately protected, the court may approve the relevant portion of the group insolvency solution and grant any relief described in article 17 that is necessary for implementation of the group insolvency solution.

Notes on article 23

54. Article 23 was approved at the fifty-second session of the Working Group as drafted (A/CN.9/931, para. 52); the word "commitment" has been replaced with the word "undertaking". See the note on relief under article 13 above. The Working Group may wish to consider whether words "the planning" in paragraph 1 might be replaced by the word "that" as indicated and the words "or will be" might be added in paragraph 2 as indicated.

United Nations A/CN.9/WG.V/WP.159

General Assembly

Distr.: Limited
1 March 2018

Original: English

United Nations Commission on International Trade Law
Working Group V (Insolvency Law)
Fifty-third session
New York, 7–11 May, 2018

Insolvency of micro, small and medium-sized enterprises

Note by the Secretariat

Contents

		Page
I.	Introduction	2
II.	Core provisions of the Guide as they relate to MSME insolvency	3
	A. Liquidation	3
	B. Reorganization	6
	C. Discharge	11
	D. Related persons and third party guarantors	13
III.	MSME issues not considered in the Guide	15

V.18-00985 (E)

Please recycle

I. Introduction

1. At its forty-sixth session (2013), the Commission requested Working Group V to conduct a preliminary examination of issues relevant to the insolvency of MSMEs, and in particular to consider whether the UNCITRAL Legislative Guide on Insolvency Law (the Guide) provided sufficient and adequate solutions for MSMEs.

2. At its forty-fifth session (April 2014), Working Group V agreed that (i) the issues facing MSMEs were not entirely novel and solutions should be developed in light of the key insolvency principles and the guidance provided by the Guide (see A/CN.9/WG.V/WP.121); (ii) it was not necessary to wait for the results of the work being done by Working Group I in order to commence the study of insolvency regimes for MSMEs; and (iii) while the work might form an additional part to the Guide, no firm conclusion on that point could be reached in advance of a thorough analysis of the issues.

3. At its forty-seventh session (2014), the Commission gave Working Group V a mandate to undertake work on the insolvency of MSMEs as a next priority, following completion of the work on the cross-border insolvency of enterprise groups and recognition and enforcement of insolvency-related judgments.

4. At its forty-ninth session (May 2016), Working Group V (i) noted the importance of MSME insolvency and the wide support that had been expressed in favour of work being undertaken on that topic; and (ii) recommended that the Commission clarify the mandate given at its forty-seventh session to Working Group V as follows: "Working Group V is mandated to develop appropriate mechanisms and solutions, focusing on both natural and legal persons engaged in commercial activity, to resolve the insolvency of MSMEs. While the key insolvency principles and the guidance provided by the UNCITRAL Legislative Guide on Insolvency Law should be the starting point for discussions, the Working Group should aim to tailor the mechanisms already provided in the Legislative Guide to specifically address MSMEs and develop new and simplified mechanisms as required, taking into account the need for those mechanisms to be equitable, fast, flexible and cost efficient. The form the work might take should be decided at a later time based on the nature of the various solutions that were being developed."

5. At its forty-ninth session (2016), the Commission clarified the mandate of Working Group V in accordance with the wording quoted in paragraph 4.

6. At its fifty-first session, Working Group confirmed that work could proceed by examining each of the topics addressed in the Guide and considering whether the treatment provided was appropriate and necessary for an MSME insolvency regime, building upon the brief outline provided in A/CN.9/WG.V/WP.121. If such treatment was not appropriate, consideration should be given to how it might need to be adjusted for MSME insolvency. Additionally, consideration should be given to issues not covered by the Guide that should nevertheless be addressed in an MSME insolvency regime. The Working Group also expressed interest in considering how the modular approach might contribute to the arrangement of the elements required for an effective and efficient insolvency regime for MSMEs.

7. This note, which should be read in conjunction with A/CN.9/WG.V/WP.121 and A/CN.9/WG.V/WP.147 addresses issues relevant to the insolvency of MSMEs, by reference to the Guide. Given that MSMEs can be found across a very wide and heterogeneous spectrum, no common definition is attempted here. Nonetheless, it is clear that all forms of MSMEs would fall within the scope of the Guide, which covers all debtors, whether legal or natural persons, engaged in economic activity.[1]

[1] Legislative Guide, introduction, para. 1.

II. Core provisions of the Guide as they relate to MSME insolvency

A. Liquidation

8. In order to identify, protect and liquidate the limited assets of the MSME debtor while minimizing further losses, key issues for consideration include:

(a) Access to low-cost and swift liquidation proceedings;

(b) Treatment of assets that may constitute or be excluded from the insolvency estate;

(c) Funding the administration of liquidation proceedings; and

(d) Resolving the above issues to provide a fresh start.

1. Access by MSME debtors

9. Recommendation 15 of the Guide presents two alternative standards for commencement of liquidation proceedings: the debtor is or will be generally unable to pay its debts as they mature (the cessation of payments test); or the debtor's liabilities exceed the value of its assets (the balance sheet test). Where a single test is adopted, it should be based on the cessation of payments test and not the balance sheet test.

10. Since many informal MSMEs do not maintain proper records, the balance sheet test may be impractical and the inconvenience of filing financial documents can act as a disincentive for MSMEs to seek timely commencement. Moreover, personal assets and liabilities are likely to be mingled with business assets and liabilities, particularly where the MSME debtor is a natural person. Where the business is doing poorly but the individual debtor is asset-rich, a balance sheet analysis could preclude access to liquidation. Given the prevalence of personal guarantees used for borrowing by MSMEs, the balance sheet analysis could be under-inclusive if it fails to reflect the liabilities of the individuals behind MSMEs.

11. The cessation of payments test may be more workable in comparison. As discussed in the Guide (part two, chapter I, paras. 23, 33 to 34), the law may accept a financial declaration from the debtor that it is unable or does not intend to pay its debts; specify the indicators of the debtor's inability to pay its debts; or establish a presumption to that effect when the debtor suspends payment of its debts. However, the cessation of payments test may face the same problem with accurately assessing an MSME's state of solvency if it fails to capture personal debts that may be intertwined with business debts.

12. Several alternative approaches to determining access, involving objective or subjective indicators, may be considered. Objective indicators may be tied to debt levels, the value of income and/or assets available, or debt-to-income ratios, using minimum and/or maximum thresholds that differ from State to State. Subjective indicators may require the debtor to demonstrate "good faith", reasonableness, or that the debts are caused by events beyond a debtor's control or not caused intentionally or through gross negligence. Access may also be dependent on factors such as the debtor's ability to cover the administrative costs of the proceedings (see paras. 23–25 below).

13. Whichever test is adopted, the overarching consideration is that the burden of proving insolvency should not be so time-consuming or difficult that MSME debtors would avoid or delay seeking commencement of liquidation proceedings. Moreover, an holistic approach to assessing MSME insolvency is desirable, so that personal assets, liabilities or guarantees used by natural persons to support MSME business are included. Likewise, as noted in the Guide (part two, chapter VI, para. 12), where a legal system distinguishes business debts from personal debts, it may not be feasible to apply different rules. This is particularly true in the context of natural persons

operating MSMEs, where business and personal debts are often intertwined. A procedure dealing with both types of debts might therefore be desirable. A procedure for joint application for commencement and procedural coordination of related proceedings might also be useful where MSME involves family members.

14. The most liberal approach would be to enable MSME debtors to access liquidation proceedings without having to declare or prove any particular financial state.[2] Lowering the barriers to access and removing the stigma of declaring insolvency can encourage timely action, provided safeguards against abuse are in place.

15. One safeguard might be to restrict the frequency of access by either preventing multiple applications by the same debtor within a certain time period or subjecting a repeated applicant to more intense scrutiny, with commencement permitted only in exceptional circumstances. Other solutions involve review and potential sanction of the debtor's conduct by permitting creditors and other interested persons to raise objections with the court.[3]

2. Assets constituting the insolvency estate

16. The Guide (recommendations 38 and 109) deals with assets that might be excluded from the estate where the debtor is a natural person. Those recommendations are not only applicable to a MSME debtor who is a natural person, but should also apply where the MSME debtor is a legal person but its business assets are intertwined with the personal assets of a natural person. In the latter case, the natural person conducting MSME may be effectively exposed to personal insolvency and should, therefore, be afforded the same protection.

17. Three possible approaches to asset exclusion might be identified.

18. First, the law may set aside a range of assets with a total value up to a specified limit, which the debtor may seek to have excluded from the estate. This means that all of the debtor's qualified assets automatically become property of the estate, and the burden is on the debtor to apply to the court for exclusion. The range of assets available for exclusion may include, for example, furniture, household equipment, bedding, clothing and tools of trade.

19. Second, the law may establish different categories of excluded assets, respectively capped at certain values. This approach may be more flexible than the first approach. The categories of assets that are relevant may differ according to the individual situation of the debtor. In some systems, if the debtor does not use up the exclusion limit in one category of assets (e.g., the family home), the law may allow application of the unused amount to other categories of assets. Other systems allow the debtor to sell off some assets to buy excluded assets.

20. Third, the law may take a more general standards-based approach that, unlike the other two approaches, excludes the debtor's assets from the estate by default and places the burden on the insolvency representative to object to the exclusion of particular assets. The court may order those assets to be reclaimed for the estate. Because the insolvency representative would only need to intervene if the debtor had particular assets that could be of value to creditors, it may be more efficient in some cases where there are few assets available for distribution. In other cases, however, it may require the insolvency representative to investigate the debtor's assets, especially where personal and business assets are mingled or assets have been hidden or transferred in close proximity to insolvency.

21. The use of reasonable limits with an emphasis on rehabilitating the debtor is to be encouraged and the law might grant the court discretion to increase the scope of excluded assets beyond the default limits to meet the needs of individual debtors.

---

[2] Ibid., part two, chap. I, para. 33.

[3] Ibid., chap. III, rec. 137.

Where there is evidence of bad faith or unfair conduct by the debtor, the law could allow the court to claw back assets that would otherwise be excluded.[4]

22. The law may permit business assets to be sold before personal assets. Private sales, in addition to public auctions, may be permitted to provide a choice for best realizing the value of the debtor's assets.

3. No-asset cases

23. In practice, MSMEs are more likely than other debtors to have insufficient or no assets to fund the administration of liquidation proceedings. While these "no-asset cases" are a regular phenomenon, responses have differed, as indicated in the Guide (part two, chapter I, paras. 72–75). Some laws require the court to refuse commencement or terminate the proceedings, while others provide specific mechanisms for the administration of the proceedings, including levying a surcharge on creditors to fund administration; establishing a public office or using an existing office; establishing a fund out of which the costs may be met; or appointing a listed insolvency professional on the basis of a roster or rotation system. Such mechanisms could be coupled with other measures to reduce the costs of liquidation proceedings for MSME debtors (see paras. 26–29 below).

24. Because a large number of no-asset MSME cases involves debtors who are natural persons, the treatment of those cases should address the possibility of granting a fresh start. If the court declines to commence or terminates liquidation proceedings because of lack of assets, the debtor's financial situation will remain unresolved.

25. An exception for individuals with limited assets who may otherwise be eligible for discharge could be considered.[5] In one jurisdiction, for example, an individual debtor's application for liquidation is deemed to be an application for discharge, and even if the debtor is unable to cover the costs of the proceeding, the termination of the liquidation proceeding leads to the immediate commencement of the discharge proceeding, thereby providing a speedy exit option for the debtor. The court can reduce the amount to be prepaid by the debtor to cover the costs of the proceeding. In other jurisdictions, alternatives in the form of debt relief schemes have been established, where qualifying no-asset debtors may seek discharge from their debts after a short time period (e.g. one year). However, the potential for serial bankruptcy may need to be addressed.

4. Simplified proceedings

26. Several legal systems provide a simplified or expedited form of liquidation proceedings, which tend to include shorter timelines[6] and procedural formalities, and less court supervision to save time and costs.

27. Measures to simplify the process of claims admission include reducing evidentiary requirements for proof of claims; limiting claims that need to be verified to those that are likely to be paid; referring submitted claims to an immediate creditor meeting for verification; eliminating the need for a court hearing to verify claims; and accelerating timelines for expressing objections and resolving disputed claims.[7]

28. A common problem for MSME liquidation is that a single disputed or unpaid claim is the main asset of the business. One straightforward solution might be for the court, another institution or an insolvency representative to perform a summary determination of the disputed claim, with the possibility of a full review on appeal to the court. Other options may include permitting the sale of the disputed claim at a discount, provided there is a secondary market for small claims or assigning the claim to the insolvency representative or public office, which will then be responsible for litigating and collecting the claim. The proceeding could be completed after the

[4] On avoidable transactions, see ibid., chap. II, rec. 87 and paras. 170–179.
[5] Ibid., chap. I, rec. 26(a) and para. 74.
[6] Greece: A/CN.9/WG.V/WP.147, para. 23; India: A/CN.9/WG.V/WP.147, para. 26.
[7] Greece: ibid.

MSME debtor has handed over other assets for liquidation, and not only after the litigation and collection of the disputed claim.

29. A simplified process may be achieved for distribution, particularly where the assets available are below a certain statutory limit, by, for example, reducing notice requirements; permitting the court to make a final decision in lieu of the creditors; or establishing one-time distribution as the norm, provided that additional dividends may be distributed on a discretionary basis. In the event that all creditors agree on the amounts and priorities of claims, together with the timing and method of distribution, the court may order distribution to be carried out on a consensual basis.

B. Reorganization

30. The design of a reorganization framework may be adapted and modified from part two, chapter IV of the Guide to promote MSME reorganization and could address:

(a) Early access to reorganization proceedings;

(b) Limiting costs and delays involved in reorganization; and

(c) Reducing requirements for creditor participation to address creditor passivity.

1. Early access

31. Given its preventive aim, reorganization should be available before MSME debtors become insolvent. As stated in the Guide (part two, chapter I, para. 46), the standard for commencing reorganization proceedings should be more flexible than the standard for commencing liquidation proceedings. The law may not require the MSME debtor to declare a state of insolvency when applying for reorganization, but permit commencement when there is a risk or likelihood of insolvency. This may be proved if, for example, the MSME debtor can demonstrate it is unable to overcome the economic, financial or legal difficulties it is facing.

32. There is, however, no consensus on whether MSME's viability should be a precondition for seeking reorganization. Some laws require the debtor to demonstrate that it is unable to pay debts that fall due without significantly hindering the continuation of its business, while others leave the assessment of viability to be made by creditors. To provide the court with an independent assessment of viability, the law may require the appointment of an insolvency representative or another person to investigate the debtor's affairs. In one jurisdiction, an individual self-employed debtor with no income and no assets is legally entitled to propose a "zero-plan" providing for no payments to his or her creditors (effectively a proposal to be discharged from all debts).[8]

33. The Guide (recommendation 139) addresses proposal of a reorganization plan on or after commencement of the insolvency proceeding, rather than as a first step. As the MSME debtor may not be in a position to draw up a feasible plan at an early stage, allowing proposal after commencement could facilitate early access to reorganization.[9] It may also give the debtor some "breathing space" to negotiate with creditors if a stay of enforcement actions comes into effect upon commencement.[10] These benefits are particularly significant for MSMEs, which are more susceptible to financial distress than larger businesses and less likely to recover from an extended period of financial distress once it occurs.

34. There are varying approaches to the role of creditors in the proposal of a plan, as noted in the Guide (part two, chapter IV, paras. 10, 11 and 13). These include giving the debtor an exclusive opportunity to propose a plan without the involvement of

[8] Germany: A/CN.9/WG.V/WP.147, para. 21.
[9] Legislative Guide, part two, chap. IV, para. 7.
[10] Ibid., part two, chap. II, para. 28.

creditors; giving the debtor a chance to propose a plan within a time limit, failing which the creditor(s) may propose a standalone plan; or permitting parties to propose competing plans at the same time. Other options may involve both the debtor and some or all of its creditors: the law may permit the debtor to propose a plan with the support of a creditor holding a certain proportion of the debt; or impose a duty on parties to cooperate in negotiating and proposing a plan.[11] The extent of creditor involvement at the proposal stage is closely linked to the procedure for approval of the proposed plan by the creditors or the court (see para. 47 below). In addition, it may be helpful to shorten the time period for MSME debtors to propose a plan, since they tend to have less complicated operations and financial arrangements

2. Debtor-in-possession

35. Recommendation 112 of the Guide notes that different approaches may be taken to the debtor's continuing role in the business during reorganization.

36. The emerging trend favours debtor-in-possession with an emphasis on rehabilitation of MSMEs. The justifications include that MSME owners and managers often have private knowledge about the business as well as ongoing relationships with creditors, suppliers and customers; the value at stake can be insufficient to fund the appointment of an insolvency representative; and the risk of being displaced from the helm can creates a powerful disincentive for small, family-run businesses to seek timely intervention.

37. The benefits of a debtor-in-possession approach should be weighed against the potential hazards of irresponsible or fraudulent conduct by the debtor. That may be addressed by providing, in certain circumstances, for the court to appoint an insolvency representative or other person to supervise the debtor-in-possession. In one jurisdiction, the court appoints a supervisor to oversee the debtor-in-possession's management in almost all cases of MSMEs that are not stock companies (in those cases a trustee is mandatorily appointed), while in another, the law enables the court to appoint a custodian where the individual debtor or the debtor's representative(s) was responsible for misappropriation or concealment of property or poor management that caused the MSME's financial distress.

38. The confidence of creditors should also be considered. Where the law permits involuntary commencement, the debtor may be hostile to creditors and should not be allowed to frustrate the proceeding. In such a scenario, the court may appoint an insolvency representative to take on a supervisory role or even displace the debtor or make an interim stay order preventing the debtor from taking certain actions (such as disposing of assets or incurring liabilities capped by a specific value) for a limited period of time. In considering these options, a balance may be needed between the incentives provided for the debtor to act in good faith while in control of the business and potential for abuse by creditors. Safeguards may include requiring the measure to be supported by a certain proportion of creditors. Other situations where debtor-in-possession may not be appropriate might include where the plan needs to be confirmed by the court by way of a cram-down on creditors (see para. 46 below).

3. Simplified plans

39. To meet the needs of MSMEs, basic forms and models may be provided as templates for designing a reorganization plan. Where an insolvency representative is appointed by the court, the plan should be prepared by the debtor with the insolvency representative's assistance.[12]

40. Provided the plan contains sufficient information to enable its viability to be assessed, the MSME debtor may not need to submit a disclosure statement[13] or

[11] Ibid., chap. IV, para. 8.

[12] OHADA: A/CN.9/WG.V/WP.147, paras. 29 and 30.

[13] United States of America: A/CN.9/WG.V/WP.147, para. 27; *Cf.* Legislative Guide, part two, chap. IV, recs. 141–143 and paras. 23–25.

financial information or audited documents.[14] The law may also permit an MSME debtor to use business and personal assets for the purposes of reorganization.

41. The parties affected by the plan will largely depend on the size and structure of MSME. Secured creditors holding a significant portion of the debt or that are entitled to satisfy their claims from encumbered assets that are critical to the reorganization of the business, should be involved in the plan, as should family members or close friends who have given personal guarantees or provided their personal assets as security for the MSME's debts. The need to modify shareholder rights, which may be restricted in some jurisdictions, is generally reduced in the case of MSMEs, since they may be unincorporated or, though incorporated, may be conducted through sole owners or as family businesses.

42. However, not all creditors will take an active role in ensuring their claims are included in the plan. To overcome passivity, the law may include a presumption of accuracy of the claims in the debtor's plan. For instance, one regime for rehabilitation of individuals requires the debtor to submit a list of claims to the court at the time of commencement; any claims not included are not subject to the proceeding. The burden is upon creditors to verify correct reflection of their claims and to raise objections within a stipulated time period. In the absence of timely objection, creditors are deemed to have waived their right to object, and the claims listed by the debtor will be confirmed with final and conclusive effect. Thus, deemed waiver raises the costs of creditor non-participation. Alternatively, if the law requires creditors to submit their claims, it can make participation easier by dispensing with submission of supporting evidence of the claims, unless specifically requested by the debtor, the insolvency representative (if appointed) or the court.

4. Quick approval

43. The Guide discusses (recommendations 145–154; part two, chapter IV, paras. 26–65) the process of voting on, approval or confirmation of, and challenges to a plan. Not all considerations involved in those steps will be applicable to the reorganization of MSMEs and the entire process could be simplified and shortened.

44. Requirements for the approval of the plan by creditors may be relaxed by eliminating the need for a creditor committee;[15] reducing the quorum required for a creditor meeting; dispensing with the need to convene a creditor meeting if adequate information has been provided by the debtor;[16] accepting a creditor's written consent to a plan without the need to attend a creditor meeting; permitting creditors to approve a plan by written resolution; permitting informal agreement to replace a formal voting process; or lowering the approval threshold of the plan.

45. Nonetheless, creditor apathy in MSME cases can make creditor approval difficult to obtain or a "majority" vote may reflect the decision of a random majority if most creditors did not participate. To incentivize creditor participation, a few systems rely on deemed approval, which interprets a lack of creditor opposition as implicit acceptance of the plan, rather than excluding those creditors from the quorum.[17] In other words, the plan may be approved by the actual and deemed votes of all creditors.

46. Where a plan has been approved by the requisite majority of creditors, the law may provide that the plan takes effect automatically, or require court confirmation before it becomes effective and binding upon all relevant parties. A middle ground is to require court confirmation in limited circumstances, such as where the plan affects the interests of dissenting parties. While there may not be many MSME cases in which a plan is actively opposed, the law may permit a cram-down mechanism for the court

[14] OHADA: A/CN.9/WG.V/WP.147, paras. 29 and 30.
[15] Argentina: A/CN.9/WG.V/WP.147, para. 18; United States: A/CN.9/WG.V/WP.147, para. 27. *C.f.* Legislative Guide, part two, chap. IV, rec. 129.
[16] United States: A/CN.9/WG.V/WP.147, para. 27. *C.f.* Legislative Guide, ibid., rec. 128.
[17] Germany: A/CN.9/WG.V/WP.147, para. 21.

to bind dissenting creditors to the plan, subject to certain safeguards[18] (see paras. 48–55 below). The law may also permit the court to take a more proactive role in facilitating the cram-down; in at least one civil law regime, the court may approve the plan by modifying its terms to protect the rights of dissenting creditors.

47. The need for creditors to vote on a plan may be replaced with court approval.[19] However, consistent with recommendation 137 of the Guide, affected creditors should be entitled to be heard if they wish to object to the plan. In one reorganization regime for individual debtors, unsecured creditors have the opportunity to be heard, but are not required to vote on a payment plan, and the plan becomes effective following court approval. Because both debtors and creditors that are MSMEs may not be well informed about the reorganization process and may have limited or no access to advice, the court may be the best placed decision-maker.

5. Conditions for approval

48. Recommendation 152 of the Guide sets out certain conditions to be satisfied before the court can approve or confirm a plan. Those conditions may apply whenever the court reviews a plan, or only in limited instances, such as a cram-down on dissenting creditors or a challenge to an approved plan.[20]

49. To discourage frivolous complaints and minimize delays in MSME reorganization, some laws have narrowed the scope for objections to be made on procedural grounds and the court can authorize a plan that does not strictly satisfy those grounds. For instance, the court may approve or confirm a plan, notwithstanding an objection that the approval process was not properly conducted or that the plan contains a provision contrary to law, by taking into account the extent of the irregularity in the process or the plan, the state of the MSME debtor, or other circumstances.

50. Other conditions serve to protect the interests of creditors, including that they should receive at least as much under the plan as they would have received in liquidation, unless specifically agreeing to lesser treatment (the best interest test).[21] While that test can be applied to MSME cases, the law could permit the court to determine the outcome of an alternative liquidation scenario without the involvement of expert opinion.

51. As an alternative, a more general test of fairness could be considered to simplify the reorganization proceeding and remove any need for the court to evaluate and compare alternative scenarios. Instead, the court assesses whether the interests of all creditors are sufficiently protected under the plan, such as whether the minority creditors were fairly represented at the meeting, whether the majority creditors acted in good faith, and whether the plan would be approved by a reasonable and honest person who was affected. At the same time, the court should not have to examine the substance of the commercial terms to which the majority creditors have agreed.[22] Such a test may be suitable for MSME cases, provided it can be applied with certainty.

52. Application of the absolute priority rule may need to be considered in MSME reorganization.[23]

53. The strict application of the rule may hinder implementation of the plan. Because the aim is to rescue the MSME debtor, the plan may provide for payment to creditors over several months or even years, using both current assets and future income. If senior creditors must be paid in full ahead of junior creditors, the debtor's

---

[18] Legislative Guide, part two, chap. IV, paras. 54–55.
[19] *C.f.* ibid., recs. 127, 145.
[20] Ibid., recs. 151, 153.
[21] Ibid., rec. 152(b).
[22] Ibid., para. 63.
[23] On the priority of tax claims, see ibid. chap. V, paras. 69 and 74; see also para. 72 below. On the special treatment of claims by related persons, see ibid., chap. V, paras. 48 and 77 and chap. IV, rec. 152(e); see also paras. 82–84 below.

assets may be exhausted all at once, before there is even a chance of rescue. It may thus be desirable for junior creditors to be paid before senior creditors are paid in full, provided the plan observes the relative priority between the creditors. That may create more flexibility for the parties and the court, particularly where a cram-down is needed to give effect to the plan.

54. Second, the absolute priority rule renders creditors that are MSMEs (MSME creditors) especially vulnerable since, as noted above, they may require payment during the reorganization in order to continue trading. That could, in turn, jeopardize the plan where the successful reorganization of the MSME debtor depends on the survival of those creditors as its transaction partners. The law can recognize the vulnerable status of MSME creditors by placing them in a class separate from other unsecured creditors. Where the law permits court approval by way of a cram-down, that class of MSME creditors may be exempted from the cram-down. Alternatively, the law may carve out specific exceptions to the absolute priority rule by granting priority, in limited circumstances, to those creditors' claims, for instance, for goods supplied to the debtor within a specified time period before commencement of the reorganization proceeding. The law may also give the court discretion, on a case-by-case basis, to order preferential payment of MSME creditors' claims, such as where necessary for continuation of those creditors' businesses. Another approach excludes MSME creditors' claims from the plan.

55. Third, the absolute priority rule may create a disincentive for owner/managers of incorporated MSMEs to seek reorganization, because they risk losing their ownership of the business to creditors with higher priority. Consistent with the debtor-in-possession approach, MSME owners should usually be allowed to continue running the business without surrendering their ownership interests under the plan. At the same time, the law may stipulate that the plan should not allow payments to MSME owners as long as there are payments outstanding to creditors, thus respecting the priority of creditors ahead of shareholders. The court would need to assess the funds required for the MSME's survival and the disposable income available for payment. However, a wholly discretionary approach may lead to inconsistent outcomes in practice. A different approach may be a bright-line standard. For example, to protect creditors in the absence of absolute priority, the law may permit the plan to be approved or confirmed only if it provides a minimum level of payment to creditors over a certain time period. Alternatively, the law could establish a minimum standard of protected income for MSME.

6. Expedited proceedings

56. As discussed in the Guide (recommendations 160–168 and part two, chapter IV, paras. 76–94), expedited reorganization proceedings may be used to give effect to an informally negotiated plan at greater speed and lower cost.

57. The documentary requirements for commencement would differ from those applicable to full reorganization proceedings. In addition to submitting the negotiated plan, the MSME debtor would need to demonstrate the plan has received the requisite support by providing the written consent of the affected creditors or, where a creditor meeting has been held, a report of the creditors' votes.[24] As to disclosure requirements, (see para. 40 above), the same approach as taken in simplified proceedings should apply in expedited proceedings.[25]

58. The law may also reduce court supervision and waive certain requirements leading to the approval of the plan. Claims included in the plan may be admitted without examining proof of those claims;[26] the plan may be referred to an immediate creditor meeting or court hearing (as the case may be);[27] or the court may directly confirm the plan with final and binding effect. Once the plan is confirmed by

[24] Ibid., part two, chap. IV, rec. 162(d).
[25] *C.f.* Ibid., recs. 162(a) and (e).
[26] *C.f.* Ibid., recs. 165(b)-(c).
[27] Ibid., rec. 164(d).

the court, affected creditors would be bound in the same manner as in full reorganization proceedings.

7. Appeals

59. The possibility of an appeal against a court decision (e.g., on the confirmation or approval of a plan) will be influenced by concerns about certainty, delay and costs. Some jurisdictions do not necessarily provide a right of appeal, whereas other jurisdictions permit an appeal, but it does not have the effect of suspending implementation of the plan. The latter can be crucial for MSMEs, since the success of the plan will often depend greatly on prompt implementation. Any risk of irrecoverable loss caused by implementation of the plan may be balanced by the provision of security or other provisional measures.

60. Should the appeal succeed after the plan is implemented, however, setting aside or unravelling the plan may cause more harm than good to all parties involved. As an alternative, the court may be authorized to order the debtor to pay monetary compensation to dissenting creditors or creditors who voted in favour of the plan.

8. Conversion to liquidation

61. Recommendation 158 of the Guide states that the law should permit the court to convert reorganization to liquidation proceedings on five grounds.

62. In the event that full reorganization proceedings are unsuccessful due to grounds (a)–(d), it may be appropriate for the law to allow automatic conversion to liquidation proceedings, avoiding the delay and expense of a separate application by either the MSME debtor or creditors. However, as noted in the Guide (recommendation 168 and part two, chapter IV, para. 91), conversion may not be appropriate where MSME commenced expedited reorganization proceedings to address financial difficulties at an early stage, but was not necessarily eligible for liquidation proceedings.

63. The possibility of allowing a creditor to pre-emptively apply for conversion, on the ground that the debtor's plan is doomed to fail, may also be considered.

64. There may be other circumstances which could affect the debtor's ability to implement the plan. One State provides that, if an individual debtor has paid at least 75 per cent of their debts according to the plan and it becomes difficult to continue payment for reasons beyond the debtor's control, the court may grant a "hardship discharge".

C. Discharge

65. Discharge is another core element of MSME insolvency. As noted in the Guide (part two, chapter VI, para. 1), several States have recognized the need to focus on facilitating a fresh start for insolvent debtors after resolving their financial difficulties and reducing the stigma associated with business failure.

66. Recommendations 194 to 196 of the Guide concern discharge where the debtor is a natural person. These recommendations are generally applicable to MSMEs conducted through natural persons, whether as sole proprietors or in a group, such as a partnership, association or other unincorporated entity, which exposes them to personal liability for unpaid debts. As for MSMEs conducted through companies and other legal entities with limited liability, the owners and managers of the liquidated entity will not be personally liable for unsatisfied claims per se.[28] Nonetheless, many of these individuals may have incurred personal debts for their business activities by taking personal loans to start and run the business or may have guaranteed business loans with personal assets. In such cases, the question of discharge arises as a result of the mixing of business and personal debts.

[28] Ibid., chap. VI, para. 3.

1. Quick discharge

67. The most debtor-friendly approach is to permit a full discharge (or "straight" discharge) of debt immediately following distribution in liquidation. This is offered in some legal systems and grants complete debt relief to the debtor without requiring a payment plan. For example, the law may provide for an immediate discharge following a brief evaluation and possible liquidation of the debtor's assets or if the court determines the debtor's circumstances make it clear no distribution to creditors can reasonably be expected.

68. The need to balance the interests of the debtor and creditors has led many insolvency regimes to stipulate a period of time that must elapse before an honest and cooperative debtor can obtain a full discharge. This approach can be combined with a reorganization plan, which ensures that the discharge is conditional on partial repayment or, at least, on good faith efforts to make repayment. The starting point of the discharge period may differ; it may be pegged to the commencement of the liquidation proceeding, to conversion of a reorganization into a liquidation (see paras. 61–64 above) or, where there is a reorganization plan, to the court's approval of the plan or to its commencement or completion date. The length of the discharge period varies from jurisdiction to jurisdiction, but the emerging trend is to shorten the discharge period to encourage entrepreneurial activities and reduce stigma.

69. Where the discharge is conditional on partial repayment, the law may ensure the repayment obligation is not overly onerous by requiring, for example, that the repayment obligation is based on each debtor's situation and is proportionate to disposable income over the discharge period. Another approach is to establish a sliding scale which calibrates the length of the discharge period according to the rate of return to creditors; the more the debtor is able to pay, the sooner they will obtain a discharge. The law may also provide for exceptional circumstances in which a debtor may apply to the court for a discharge (see para. 64 above).

70. In terms of procedure, discharge may take place either automatically or upon application to the court. The former is more expeditious, eliminating the need for judicial intervention. The latter may be required if automatic discharge is unconstitutional or if some judicial supervision is preferred. Following discharge, claims that have not been satisfied would be rendered unenforceable.

71. The benefits of a quick discharge are more pronounced in the context of MSME insolvency, particularly where the debtor is towards the "micro" end of the spectrum. Due to MSMEs' limited resources, creditors often do not expect to receive substantial returns and may have written off the claims long before the expiry of the discharge period. At the same time, a shorter discharge period incentivizes the debtor to seek timely commencement of the insolvency proceeding and to comply with obligations to creditors as far as possible in order to obtain an early discharge.

2. Scope of discharge

72. The effectiveness of a discharge regime in achieving the debtor's rehabilitation depends on the scope of debts covered by the discharge. Certain types of debt, such as debts based on tort claims, maintenance obligations, fraud, criminal penalties, and taxes, tend to be excluded from discharge.[29] Some countries, however, have eliminated special treatment for taxes and other public revenue claims, which are often among the largest debts of small business owners. This is in line with recommendation 195 of the Guide, which states that the exclusion of debts from a discharge should be kept to a minimum in order to facilitate a fresh start.

73. Given the likelihood that business and personal debts are intertwined, it may be burdensome for an MSME debtor to apply for separate procedures to discharge all debts, especially if they have different criteria and discharge periods. As noted above (see para. 13), it is desirable that both types of debt can be dealt with in a single

[29] Ibid., chap. VI, para. 7.

discharge regime or, at least, that separate proceedings may be consolidated. It may also be possible to consider a reduction of the debtor's personal guarantee as a de facto discharge, without necessarily declaring the debtor bankrupt, so as to facilitate the debtor's fresh start.

3. Conditions for discharge

74. To provide safeguards against abuse, the insolvency law can regulate the availability of a discharge or the length of a discharge period in specific circumstances, although such conditions should be kept to a minimum, as stated in the Guide (recommendation 196). In addition, a key feature of the MSME-specific approach is a presumption of honesty. This grants the debtor the benefit of a discharge unless they are proven to have acted fraudulently or in bad faith. The experience of some jurisdictions with debtor-friendly discharge regimes shows that it does not result in a rise in unpaid claims or widespread misuse of discharge options by debtors.

75. A discharge of debt may be accompanied by disqualification, which precludes the debtor from starting or carrying on a business, practising in a profession, or acting as a company director or manager. The disqualification period may be long or even indefinite or may be linked to the discharge period. Disqualification could occur automatically or upon a court order, and may be subject to carve-outs to prevent abuse. The disqualification period may be extended in exceptional situations if the debtor's conduct justifies such a sanction, such as where the debtor was guilty of criminal misconduct or otherwise ordered to be disqualified by a court in criminal proceedings.[30] For sole traders or entrepreneurs who manage their own businesses or who entered into insolvency after giving personal guarantees, a blanket disqualification may be inappropriate, since it would effectively prohibit them from being involved in future enterprises, defeating the concept of a fresh start.

76. Restrictions on obtaining new credit can also have a major impact on the debtor's ability to start afresh, particularly if the impact lasts long after the debtor's discharge. In many countries, borrowers are required to disclose whether they are or have been subject to insolvency, which can lower their credit scores or be reflected as negative entries in their credit histories, leading to discrimination against former debtors. To mitigate this, restrictions on borrowing should be imposed carefully and the period of such restrictions reduced. Such measures can be coupled with efforts beyond the formal insolvency framework, such as out-of-court restructuring with financial institutions, to provide individual debtors with the benefits of discharge without affecting their personal credit scores or the use of data protection laws to regulate the collection and retention of personal information by credit providers or bureaux.

D. Related persons and third party guarantors

77. Third parties related to the natural person conducting MSME, such as family members or close friends, can be drawn into the MSME's insolvency because they have taken on personal loans, given personal guarantees or provided their property as collateral security for business loans.[31] Since the involvement of related persons tends to be more ubiquitous in MSMEs than in larger enterprises, their position under insolvency law merits consideration in greater detail.

78. In addition, competing policies have to be weighed in the treatment of third party guarantors in MSME cases. On one hand, the purpose of requiring a personal guarantee or security is precisely to hedge against the principal debtor's insolvency by ensuring the creditor will get paid. Adjusting the guarantor's liability in the insolvency proceeding would reduce the protection for the creditor. This could, in the

[30] Ibid., para. 9.

[31] Ibid., Introd., see subpara. 12(jj): for the definition of a "related person". On levels of connection to the debtor see part two, chap. II, para. 183.

long run, restrict access to credit for MSMEs, many of which may not be able to obtain financing in other ways. On the other hand, where the MSME's insolvency implicates family members or household assets, allowing unrestricted enforcement of guarantees could leave an entire family destitute.

79. Several aspects of the Guide deal with related persons, recommending that the law should specify the categories of persons with sufficient connection to the debtor to be treated as related persons;[32] any proposed disposal of an asset to a related person should be carefully scrutinized before being allowed to proceed;[33] the suspect period for avoidable transactions involving related persons may be longer than for transactions with unrelated persons;[34] related persons may not be eligible for appointment to a creditor committee;[35] claims by related persons should be subject to scrutiny and, where justified: (a) the voting rights of the related person may be restricted; (b) the amount of the claim of the related person may be reduced; or (c) the claim may be subordinated;[36] and the related persons whose claims have been denied or subjected to such treatment should be permitted to request the court to review their claims.[37] The Guide does not address third party guarantors, apart from noting that the discharge of a natural person debtor generally does not affect the liability of the guarantor.[38]

80. One issue for consideration is whether the law should permit a court to extend the reach of a stay (Guide, part two, chapter II, recommendation 46; paras. 30–34) to protect the guarantor of an MSME debtor. Staying enforcement against the guarantor, whose role is often crucial to the financing of MSME, can assist in the successful reorganization of the MSME debtor. It would extend the scope of the "breathing space" for a rational decision to be made collectively about the entirety of the MSME debtor's obligations and affairs.

81. Any extension of a stay to guarantors would, however, be an extraordinary departure from the usual approach in business insolvency cases and should be restricted to appropriate circumstances. For example, the benefit of a stay may be granted by the court on a case-by-case basis where it is deemed necessary to protect a related person guarantor that has provided a personal guarantee without receiving any consideration. Further, the stay of enforcement against guarantors may be limited to a short time period, following which creditors are free to take action. In any event, to protect the rights of creditors, the court may permit enforcement against guarantors who demonstrate bad faith or unfair conduct, such as by hiding property.

82. As to the treatment of claims by related persons, the Guide acknowledges (part two, chapter V, para. 48) that the mere fact of a special relationship with the debtor may not be sufficient in all cases to justify special treatment of a creditor's claim. In some cases, the claim will be entirely transparent and should be treated in the same manner as similar claims made by creditors who are not related persons. In other cases, the special relationship may give rise to doubts regarding whether the related person creditor will be impartial when voting on a reorganization plan or whether the debtor unfairly favoured the related person creditor over other creditors before the onset of insolvency. In one system, the claim of a related person who received a cash loan from the MSME debtor or became a guarantor for the MSME debtor may be subordinated to other claims in the plan.

83. Considerations of proportionality and potential hardship to the MSME debtor's guarantor may, however, justify giving the court discretion to favour the guarantor's claim when approving or confirming a reorganization plan, or permitting the guarantor to apply for an extended payment period to alleviate the guarantee

[32] Ibid., chap. II, rec. 91.
[33] Ibid., rec. 61.
[34] Ibid., rec. 90.
[35] Ibid., chap. III, rec. 131.
[36] Ibid., chap. V, rec. 184.
[37] Ibid., rec. 181.
[38] Ibid., chap. VI, para. 13.

obligation. Such measures may be appropriate where the guarantor has made great sacrifices to pay the debt and the other creditors are institutions. Similar considerations may support an exercise of discretion in favour of the guarantor's discharge.

84. The need to provide debt relief to related persons who face insolvency because they provided personal guarantees for the MSME business, especially in cases where a reduction or discharge of their obligations was not achieved through a reorganization plan, could be factored into the discharge regime. Although the guarantor can apply for relief separately, providing standing to apply for relief in the proceeding concerning the MSME debtor could be a more cost-efficient approach and more consistent with the aim of providing a fresh start to the MSME debtor, particularly if it mitigated the potentially undesirable consequences of enforcing the guarantee. One legal system permits natural persons and gratuitous sureties to petition for a discharge of the surety's obligation that is implicated in the principal's insolvency if that obligation is disproportionate to the surety's revenue and patrimony.

III. MSME issues not considered in the Guide

85. As noted above (para. 4), the Working Group's mandate includes, in addition to considering the applicability of the Guide to MSMEs, the development of new and simplified mechanisms for MSMEs as required. Document A/CN.9/WG.V/WP.121, paragraph 33 raises several issues not addressed in the Guide, such as personal insolvency, treatment of group debt, use of informal insolvency processes and debt adjustment mechanisms. The Working Group may wish to identify additional issues relevant to MSME insolvency that should be addressed in any work product to be developed.